In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 318

ESTATE OF ARTHUR SWEET, DECEASED, TRACY-COLLINS TRUST COMPANY, ADMINISTRATOR, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The findings of fact and opinion of the Tax Court (R. 29–39) are reported at 24 T. C. 488. The opinion of the Court of Appeals (Pet. App. 1–6) is reported at 234 F. 2d 401.

JURISDICTION

The judgment of the Court of Appeals was entered on May 26, 1956. Taxpayer's petition for rehearing was denied on June 28, 1956. The petition for a writ of certiorari was filed on August 15, 1956. The jurisdiction of this Court is invoked under 28 U. S. C. 1254.

QUESTIONS PRESENTED

1. Whether the courts below erred in construing two trust agreements as creating one trust only.

2. Whether on the facts of this case the courts below were bound by the judgment of the District Court of the State of Utah that two separate trusts were created.

STATUTE AND REGULATIONS INVOLVED

The relevant statute and regulations, Section 812 (e) (1) of the Internal Revenue Code of 1939, and Section 81.47a (e) of Treasury Regulations 105, are set forth in the Appendix, *infra,* pp. 9–11.

STATEMENT

On June 6, 1947, Arthur Sweet, the decedent, executed a revocable trust agreement, with Tracy-Collins Trust Company as trustee. It provided in substance that the trustee should pay the income to the trustor for his life, and thereafter to his wife, for her life, and that, upon the death of both, the trust should terminate and the trust estate be distributed equally to his four children, with further provision for payment in a specific manner in the event of the death of any of the children before termination of the trust. (R. 19–24.)

In July, 1948, the decedent was advised that there would be a substantial savings in estate tax if Mrs. Sweet were given a power of appointment over one-half of the trust estate. (R. 31.)

On July 27, 1948, the trustor executed an instrument denominated "Supplemental Trust Agreement."

This instrument provided for the cancellation of paragraph IV of the original agreement and substituted a new paragraph therefor. The substituted paragraph provided that the trustor's wife should (R. 25)—

> have the power of appointment over such portion of the Trust Estate as equals one-half (½) of the value of my adjusted gross estate, as appraised for federal estate tax purposes. The power of appointment of the said Margaret M. Sweet shall be exercisable in favor of herself, or in favor of her estate, or in favor of any other person, whom she shall elect to appoint. * * * In the absence of an appointment completely disposing of said portion of the Trust Estate, upon the death of said Margaret M. Sweet, said portion of the Trust Estate shall terminate and the Trustee shall pay, disburse and distribute the same, in equal shares, unto the daughter of the Trustor, Dorothy Sweet Hindin, the daughter of the Trustor, Barbara Sweet Hartman, the daughter of the Trustor, Margaret "Peggy" Sweet, and the son of the Trustor, Arthur David Sweet.

The "Supplemental Trust Agreement" further provided that (R. 25)—

> The Remainder of the Trust Estate, over which the said Margaret M. Sweet has no power of appointment, shall terminate upon the death of the last survivor of the Trustor, and said Margaret M. Sweet * * *.

Provisions for the event that a child should predecease the trustor or his wife (R. 26) were identical with those in the original agreement (R. 21–22). The

"Supplemental Trust Agreement" provided further that (R. 26)—

> Except as herein specifically amended, modified or changed, the said Trust Agreement dated June 6, 1947, is hereby ratified and confirmed in all respects and particulars.

In administering the trust agreements, the trustee established and maintained records for only one trust, and filed only one fiduciary return in each of the years 1948 to 1951. (R. 32.)

Arthur Sweet died on September 29, 1948. (R. 30.)[1] A marital deduction from the gross estate of the decedent was claimed under Section 812 (e) (1) (F) of the Internal Revenue Code of 1939, as added by Section 361 of the Revenue Act of 1948, c. 168, 62 Stat. 110. The Commissioner disallowed the claimed deduction and imposed a resulting deficiency. Taxpayer filed a protest against the proposed deficiency on November 24, 1951. (R. 33.)

The controversy was over the question whether the trust agreement and supplemental trust agreement created one trust only or two separate trusts. It has been agreed in the courts below and here (Pet. 3) that if there were two separate trusts, the one over which Mrs. Sweet had the power of appointment would qualify for the marital deduction, and, on the other hand, that if only one trust was created taxpayer was not entitled to the marital deduction for the reason that the surviving wife's power

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[1] The opinion of the court below (Pet. App. 2) erroneously states this date as October 21, 1952.

of appointment did not extend to the entire corpus of the trust as required by statute.

On August 22, 1952, ten days after a conference with the representatives of the Commissioner on this issue (R. 8), taxpayer filed a complaint in the District Court of the Third Judicial District of Utah, requesting that court to interpret and construe the instruments as creating two separate trusts. (R. 33.) The decedent's wife and four children were named as defendants and given notice of the action. They filed an appearance but failed to answer or otherwise plead to the complaint and did not appear either in person or by counsel. At the trial taxpayer appeared by its attorney. The court rendered its judgment the same day, determining in almost the exact language of the suggestions set forth in the complaint that the original trust agreement and the supplemental agreement created two separate and distinct trusts. (R. 33–34, 36.)

The courts below concluded on the facts that the proceeding in the state court was instituted with the concurrence of the trustee and the beneficiaries under the trust for the sole purpose of circumventing the contention of the Commissioner that the trustor did not create two separate and distinct trust estates; that it was nonadversary in character and there was no real controversy between the parties and that the decision of the state court amounted to a consent decree. (R. 36–37; Pet. App. 5–6.)

Taxpayer then filed its petition in the Tax Court seeking a redetermination of the estate tax deficiency. (R. 3–6.) That court held that the trust instru-

ments showed an intention by the deceased to create only one trust and that it was not bound by the decision of the state court. (R. 35–39.) The Court of Appeals affirmed.

ARGUMENT

1. In interpreting the trust agreements the court below construed the two instruments together, and held that the supplemental agreement did not indicate a purpose to create two separate trusts. It pointed out that the agreement speaks throughout of the trust in the singular, not the plural, that it vests in the surviving spouse a power of appointment over a "portion" of "the Trust Estate," that upon the death of the trustor and his wife "the remainder of the trust estate" shall terminate.

In looking at the entire instrument to determine the trustor's intent and in giving weight to the use of the singular instead of the plural, the court here used the same method of interpretation as was followed in the cases cited by taxpayer (Pet. 10). Taxpayer asserts that there is no uniformity as to rules of interpretation followed by the different Courts of Appeals (Pet. 10). On the contrary, the courts, in the cases cited, are in substantial agreement as to the rules of interpretation. Those rules, applied to different trust instruments, have resulted in different conclusions as to whether there were several trusts or but one, the different conclusions arising not from varying rules of interpretation but from variances in the trust instruments.

The court below correctly applied those rules. Taxpayer is merely seeking a third judicial construc-

tion of a particular trust instrument. Review by this Court is not warranted, especially since similar problems in connection with the marital deduction are unlikely to arise in the future, the rule applicable to such cases having been changed by Congress by Section 2056 (b) (5) of the Internal Revenue Code of 1954.

2. The court below refused to give effect to the state court judgment that there were two separate trusts on the grounds that the state court proceeding was instituted for the single purpose of circumventing the ruling of the Commissioner that the trustor did not create two separate trust estates, that it was nonadversary in character, and that the decree was obtained by collusion for the purpose of maintaining the claim for marital deduction.

Taxpayer (Pet. 9–10) objects to this statement as to the collusive nature of the decree as unsupported by the evidence. It is apparent, however, that the Court of Appeals used the term as defined by this Court in *Freuler* v. *Helvering,* 291 U. S. 35, 45, as "collusive in the sense that all the parties joined in a submission of the issues and sought a decision which would adversely affect the Government's right to additional income tax." The record supports the court's holding that there was collusion in this special sense.

In holding that it was not bound by an order of a state court entered by collusion in a nonadversary proceeding the court below was also in accord with other Courts of Appeals. *Newman* v. *Commissioner,* 222 F. 2d 131 (C. A. 9th); *Estate of Rainger* v.

Commissioner, 183 F. 2d 587 (C. A. 9th), certiorari denied, 341 U. S. 904; *Green* v. *Commissioner,* 168 F. 2d 994 (C. A. 6th); *Saulsbury* v. *United States,* 199 F. 2d 578 (C. A. 5th), certiorari denied, 345 U. S. 906.

Contrary to taxpayer's contention (Pet. 7) the decision below is not in conflict with the decision of the Court of Appeals for the Third Circuit in *Gallagher* v. *Smith,* 223 F. 2d 218, for there the Third Circuit plainly agreed with the courts below here that a state court judgment obtained by collusion to defeat a federal tax need not be given conclusive effect in a suit in a federal court involving that tax, and the nonadversary character of a state suit is undoubtedly relevant as evidence of such collusion (p. 225).

CONCLUSION

The decision of the court below is correct, is in accord with the applicable decisions of this Court, and is not in conflict with the decision of any other Court of Appeals. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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SEPTEMBER 1956.

APPENDIX

Internal Revenue Code of 1939:

SEC. 812. NET ESTATE.

For the purpose of the tax the value of the net estate shall be determined, in the case of a citizen or resident of the United States by deducting from the value of the gross estate—

* * * * *

(e) [as added by Sec. 361 of the Revenue Act of 1948, c. 168, 62 Stat. 110] *Bequests, Etc., to Surviving Spouse.*—

(1) *Allowance of marital deduction.*—

(A) *In General.*—An amount equal to the value of any interest in property which passes or has passed from the decedent to his surviving spouse, but only to the extent that such interest is included in determining the value of the gross estate.

* * * * *

(F) *Trust with Power of Appointment in Surviving Spouse.*—In the case of an interest in property passing from the decedent in trust, if under the terms of the trust his surviving spouse is entitled for life to all the income from the corpus of the trust, payable annually or at more frequent intervals, with power in the surviving spouse to appoint the entire corpus free of the trust (exercisable in favor of such surviving spouse, or of the estate of such surviving spouse, or in favor of either, whether or not in each case the power is exercisable in favor of others), and with no power in any other person to appoint any part of the corpus to any person other than the surviving spouse—

(i) the interest so passing shall, for the purposes of subparagraph (A), be considered as passing to the surviving spouse, and

(ii) no part of the interest so passing shall, for the purposes of subparagraph (B) (i), be considered as passing to any person other than the surviving spouse. This subparagraph shall be applicable only if, under the terms of the trust, such power in the surviving spouse to appoint the corpus, whether exercisable by will or during life, is exercisable by such spouse alone and in all events.

* * * * *

(H) *Limitation on Aggregate of Deductions.*—The aggregate amount of the deductions allowed under this paragraph (computed without regard to this subparagraph) shall not exceed 50 per centum of the value of the adjusted gross estate, as defined in paragraph (2).

* * * * *

(26 U. S. C. 812.)

Treasury Regulations 105, promulgated under the Internal Revenue Code of 1939:

SEC. 81.47a [as added by T. D. 5699, 1949-1 Cum. Bull. 181]. *Bequests, Etc., to Surviving Spouse.*—(a) *Allowance of marital deduction.*— * * *

* * * * *

(c) *Trust with power of appointment in surviving spouse.*—In the case of property interests which passed from the decedent to a trust, the terms of which satisfy the five conditions stated in this paragraph, the expression "passed from the decedent to his surviving spouse" embraces not only the beneficial interest therein of such spouse but also the interest therein

subject to her power to appoint. * * * The five conditions which must be satisfied by the terms of the trust are as follows:

> (1) The surviving spouse must be entitled for life to all the income from the corpus of the trust.
>
> (2) Such income must be payable annually or at more frequent intervals.
>
> (3) The surviving spouse must have the power, exercisable in favor of herself or of her estate, to appoint the entire corpus free of the trust.
>
> (4) Such power in the surviving spouse must be exercisable by such spouse alone and (whether exercisable by will or during life) must be exercisable in all events.
>
> (5) The corpus of the trust must not be subject to a power in any other person to appoint any part thereof to any person other than the surviving spouse.
>
> * * * * *

If the surviving spouse is entitled to only a portion of the trust income, or has power to appoint only a portion of the corpus, the trust fails to satisfy conditions (1) and (3), respectively. However, such conditions may be satisfied by one or more of several separate trusts created by the decedent. An undivided interest in property may constitute the corpus of a trust, and the will or a single trust instrument may create more than one trust.

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U. S. GOVERNMENT PRINTING OFFICE: 1956